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WM.N - Q4 2020 Waste Management Inc Earnings Call

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OVERVIEW:

WM reported 4Q20 results. Expects 2021 revenues to grow 10.75-11.25%.

CORPORATE PARTICIPANTS

Devina A. Rankin *Waste Management, Inc. - Executive VP & CFO*

Edward A. Egl *Waste Management, Inc. - Director of IR*

James C. Fish *Waste Management, Inc. - President, CEO & Director*

John J. Morris *Waste Management, Inc. - Executive VP & COO*

CONFERENCE CALL PARTICIPANTS

David John Manthey *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Hamzah Mazari *Jefferies LLC, Research Division - Equity Analyst*

Jeffrey Daniel Goldstein *Morgan Stanley, Research Division - Research Associate*

Jeffrey Marc Silber *BMO Capital Markets Equity Research - MD & Senior Equity Analyst*

Kevin Chiang *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

Kyle White *Deutsche Bank AG, Research Division - Research Associate*

Michael Edward Hoffman *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Michael J. Feniger *BofA Securities, Research Division - VP*

Noah Duke Kaye *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Patrick Tyler Brown *Raymond James & Associates, Inc., Research Division - MD*

Sean D. Eastman *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

Stephanie L. Yee *JPMorgan Chase & Co, Research Division - Analyst*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Waste Management's Fourth Quarter and Full Year 2020 Earnings Release Conference Call. (Operator Instructions)

I would now like to hand the conference over to your host, Mr. Ed Egl. Sir, the floor is yours.

Edward A. Egl - *Waste Management, Inc. - Director of IR*

Thank you, Lara. Good morning, everyone, and thank you for joining us for our fourth quarter 2020 earnings conference call. With me this morning are Jim Fish, President and Chief Executive Officer; John Morris, Executive Vice President and Chief Operating Officer; and Devina Rankin, Executive Vice President and Chief Financial Officer. You'll hear prepared comments from each of them today: Jim will cover high-level financials and provide a strategic update; John will cover an operating overview; and Devina will cover the details of the financials, including our 2021 outlook.

Before we get started, please note that we have filed a Form 8-K this morning that includes the earnings press release and is available on our website at www.wm.com. The Form 8-K, the press release and the schedules of the press release include important information.

During the call, you will hear forward-looking statements, which are based on current expectations, projections or opinions about future periods. All forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially. Some of these risks and uncertainties are discussed in today's press release and our filings with the SEC, including our most recent Form 10-K and subsequent Form 10-Qs.

John will discuss our results in the areas of yield and volume, which, unless otherwise noted, are more specifically references to internal revenue growth, or IRG, from yield or volume. During the call, Jim, John and Devina will discuss operating EBITDA, which is income from operations before depreciation and amortization.

Any comparisons, unless otherwise stated, will be with the fourth quarter of 2019. Net income, EPS, operating EBITDA and margin and SG&A expenses have been adjusted to enhance comparability by excluding certain items that management believes do not reflect our fundamental business performance or results of operations, including costs incurred in connection with our fourth quarter acquisition of Advanced Disposal Services or ADS. These adjusted measures, in addition to free cash flow, are non-GAAP measures, please refer to the earnings press release and tables, which can be found on the company's website at www.wm.com for reconciliations to the most comparable GAAP measures and additional information about our use of non-GAAP measures and non-GAAP projections. Additionally, reconciliations for our prior 6 quarters of adjusted operating EBITDA are included in the table to the earnings press releases for those respective quarters and can also be found on our website at www.wm.com.

This call is being recorded and will be available 24 hours a day beginning approximately 1:00 p.m. Eastern Time today until 5:00 p.m. Eastern Time on March 4. To hear a replay of the call over the Internet, access Waste Management's website at www.wm.com. To hear a telephonic replay of the call, dial (855) 859-2056 and enter reservation code 1965816. Time-sensitive information provided during today's call, which is occurring on February 18, 2020, may no longer be accurate at the time of a replay. Any redistribution, retransmission or rebroadcast of this call in any form without the expressed written consent of Waste Management is prohibited.

Now I'll turn the call over to Waste Management's President and CEO, Jim Fish.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Thanks, Ed, and thank you all for joining us, and I hope everyone is staying safe and well. We're extremely pleased with our fourth quarter and our full year 2020 results. In many ways, our fourth quarter was a continuation of our strong third quarter performance. Once again, despite the impacts from the pandemic, our team delivered strong and consistent operating EBITDA in the fourth quarter that exceeded the fourth quarter of 2019.

If you set aside the $38 million of operating EBITDA contribution from ADS and the $60 million fuel tax credit benefit in the fourth quarter of '19 versus 2020, our legacy WM operating EBITDA grew 4% versus Q4 of 2019. This was our seventh consecutive quarter to generate operating EBITDA of more than $1 billion, showcasing the strength and consistency of our business. In the fourth quarter, we kept our eye on the ball working together to provide reliable, high-quality service to our customers even as we welcomed a substantial number of new customers and team members following the acquisition of Advanced Disposal.

As with the third quarter, our fourth quarter operating EBITDA margin was impressively strong at 28.1% when you consider that it included 50 basis points of dilution from ADS. For the full year, 2020 matched our highest annual operating EBITDA margin of 28.4%. And excluding ADS, we set a new record with 2020 operating EBITDA margin of more than 28.5%.

So in a year where many companies have suffered significant financial impacts from the pandemic and resulting economic crisis, at Waste Management, the resilience of our people and our business model delivered full year 2020 results within 1.5% of our record-high 2019 operating EBITDA.

As we look to 2021, in addition to the strong, continuous improvement measures we're taking in our collection and disposal business, WM is in a perfect position to leverage our focus on ESG and our accelerated investments in technology to benefit all of our constituents, employees, customers, shareholders, communities and the environment. WM made the decision in March to accelerate technology spending, and we're more confident than ever that our investments in customer service digitalization, or CSD, are the right approach to propel us forward in the post-COVID world. We've made considerable progress towards transforming our business model by seamlessly connecting the front-end customer experience to our back-end processes.

Our online sales channel is growing at a triple-digit rate. Most importantly, we're receiving positive feedback from our customers. In 2021, the value creation of CSD will step up as we further differentiate our service to our customers, automated -- automate manual processes and drive further efficiencies and reliability in our operations.

On the ESG front, WM has emerged as a true leader in sustainability, and we're doing so in a manner that will benefit both shareholders and the environment. Possibly like no other year, this year's WM Phoenix Open pointed to our ability to demonstrate our expertise and leverage our brand recognition for sustainability. This was highlighted during our Sustainability Forum panel discussion with 2 other ESG-focused CEOs, Satya Nadella of Microsoft and Doug McMillon of Walmart. Following our discussion, I received a note from Doug saying, "Thanks for your leadership, Jim." His note was flattering personally to me, but it was also an important statement about where WM stands reputationally with large companies like Walmart with regard to sustainability and where we can help them and our other customers to achieve their sustainability goals. As corporations build road maps to address their own climate impacts, WM is well positioned to assist through an array of service offerings, including recycling and other beneficial uses such as composting and renewable energy generation.

Looking at the potential impact on our financials. So far in 2021, commodities are on a strong upward trajectory, and many experts believe this to be the start of a long-term trend. And as North America's largest recycler and one of the largest producers of renewable natural gas for landfill gas, WM should benefit disproportionately from that long-term trend. We're able to close the loop by using that renewable gas to power our natural gas fleet, redefine the processing business with our next-gen recycling technology enhancements and our fee-based pricing strategy, make new investments in innovative solutions for low-value commodities and expand our portfolio of renewable natural gas plants, all of which position us perfectly to benefit our shareholders over the next 3 to 5 years.

In addition to the E in ESG, we're taking the S, our social responsibility, very seriously, too. Whether it's our long-established focus on inclusion and diversity, our commitment to our employees to enhance benefits and guaranteed hours during COVID or our efforts to help the underserved and unemployed through our work with organizations like UpSpire and Concordance Academy, we believe in these causes, and we're very confident in the long-term value add for our shareholders.

It's rewarding to see that our focus on ESG as a strategic value creator for our shareholders as well as being the right thing to do is getting recognition. At the beginning of February, we were named to Fortune magazine's World's Most Admired Companies List for the third year in a row, claiming the top spot in our industry category. During the fourth quarter, we were named to CDP's prestigious A List for tackling climate change. The global environmental nonprofit recognized Waste Management for the fifth consecutive year for our actions to cut emissions, mitigate climate risks and help develop the low-carbon economy. We were also named to the Dow Jones Sustainability Indices for North America and the World. For the third year in a row, we are in the title of Sector Leader for Commercial Services & Supplies. Our view is that our strategic approach to ESG will complement our investments in technology and our core business process improvements as the key ingredients of our future success.

Last year, we laid the foundation for lowering our operating cost model and for offering greater choice to how our customers interact with us, and we completed the sizable acquisition of ADS. All of this positions us well for growth in 2021. In the year ahead, we expect to deliver organic revenue growth of 4% to 4.5% as we continue to execute on our disciplined pricing programs and expect volume growth to improve in 2021 as the impact from the pandemic lessens.

From an operating cost perspective, we've learned how to operate our business with a lower cost structure, and we remain -- we expect to retain that lower cost structure in 2021 and beyond. As a result, we anticipate overall operating EBITDA growth between 10% and 13.5% in 2021. We expect this substantial growth as we realize the value of synergies from continuing to integrate ADS and improve the profitability of its business, all while we increase our investment in CSD. The benefits from these technology investments and the full integration of ADS will provide runway for further margin expansion in the future.

In closing, we performed exceptionally well in 2020 despite the difficulties presented with COVID-19, and we're poised for another strong year in 2021. For that, I'm eternally grateful to our teammates who have made it happen this year in the face of difficult circumstances.

I'll now turn the call over to John to discuss our operational results for the quarter.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Thanks, Jim, and good morning, everyone. We're very pleased with our strong finish to 2020, both the performance of the legacy Waste Management business and our progress in integrating the ADS operations. As Jim said, our quarterly and full year results really underscore the strength and resiliency of our business model. Improving volumes, healthy pricing and better recycling performance produced organic revenue growth for the first time since the pandemic began. As expected, legacy Waste Management collection and disposal volumes improved sequentially in the fourth quarter from a decline of 5.5% in the third quarter to a decline of 2.7% in the fourth. Fourth quarter MSW volume grew 1.2% and C&D volume, excluding hurricane cleanup, grew 1.8%, both strong indicators of continued economic recovery.

While the rate of volume recovery did moderate during the quarter, we did not see a backslide when COVID cases increased in the fall. In fact, as we look at volumes in January, we're encouraged to see improvement from the lull in late November and December.

Collection and disposal yield was 2.3% in the fourth quarter, and core price was 3.2%. Adjusted for the impact of lower volume, core price would have been 3.8%. In the collection business, we continue to make progress improving the residential line of business. Our residential yield improved 60 basis points to 3.7% in the fourth quarter compared to the same period in 2019 and was up again sequentially from 3.5% in the third quarter.

Residential volumes declined 1.4% as we shed business that does not meet our return requirements. Overall, our actions to improve the residential line of business in 2020 resulted in $40 million of operating EBITDA benefit, and we expect this to carry forward into 2021.

In the post-collection business, fourth quarter landfill core price was 3.3% and transfer station core price was 3.1%, demonstrating our continued pricing discipline in these key lines of business.

Moving to costs. Operating costs were 61.5% of revenue in the fourth quarter compared to 60.2% in the fourth quarter of 2019. There were some noise in the fourth quarter results. Let me walk you through the difference. In the quarter, as expected, the ADS acquisition increased operating expense as a percentage of revenue by 40 basis points. Additionally, the timing of government approvals for fuel tax credits, which benefited the fourth quarter of 2019 with 2 years' worth of credits, resulted in a 150-basis-point headwind to operating expense as a percentage of revenue in the fourth quarter of 2020. Aside from these impacts, operating costs as a percentage of revenue improved 60 basis points, demonstrating that we are laser-focused on cost control and continue to benefit from a lower cost structure. As an example, commercial yards and industrial halls declined between 5% and 6% during the fourth quarter, yet overtime decreased in the range of 15% to 18%, and we see additional opportunities. We also have plenty of opportunity to improve operating costs as a percentage of revenue in the ADS business as we further integrate operations and work to exceed our planned synergies.

Devina will cover our 2021 financial guidance in more detail, but I want to spend a minute on some key components of growth as we look at the year ahead. We are extremely confident in the aspects of our outlook that we can control, and we based our guidance on a stabilizing economy, moderate volume growth and disciplined pricing. We expect organic revenue growth from yield and volume in the collection and disposal business of between 4% and 4.5% and overall revenue growth between 10.75% and 11.25% during 2021.

We hit the ground running on the ADS integration on October 30, and it's progressing very well. We expect to achieve between $50 million and $60 million in synergies during 2021. Combined with the $10 million to $15 million of annualized synergies already achieved in the fourth quarter, our run rate synergies exiting 2021 is expected to be between $60 million and $75 million. We are extremely confident in achieving these synergies and that we'll be able to capture the remaining synergies in the first half of 2022. About 1/3 of the 2021 synergies will come from route optimization, which will begin early in the second quarter. We estimate that our onetime cost to achieve these synergies will be $50 million in 2021. And as we've mentioned, we plan to adjust the majority of these costs from our results.

As Jim discussed, our recycling and renewal energy businesses are central to our strategy, and we're anticipating strong growth from these businesses in the year ahead. We expect continued improvement in recycling from our fee-for-service model, improved operating cost structure at new MRFs and stable demand for recycled materials, which, together, provide a tailwind of between $40 million and $50 million to 2021 operating EBITDA. We also expect an incremental $10 million of year-over-year contribution from our renewable energy business from the sale of RINs as pricing for those credits has increased over the last several months. Devina will talk more about our plans to invest in these key businesses in 2021.

In closing, I want to thank the entire Waste Management team, including our new team members from ADS, for their focus in what continues to be difficult and distracting times. The team has done an exceptional job managing our operations, and I know this will continue in the year ahead.

I'll now turn the call over to Devina to discuss our 2020 financial results and 2021 financial outlook and further detail.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Thanks, John, and good morning. Our 2020 results demonstrate strong execution from our frontline teams across North America, serving our customers throughout the pandemic and doing so in an increasingly cost-effective way. The same focused execution and cost discipline extended to our team members in sales and back-office functions, which delivered strong SG&A results for the year. Excluding $25 million of SG&A for the ADS business, SG&A improved by $56 million in 2020 to 10.2% of revenue, a 10-basis-point improvement over 2019. We achieved these results while accelerating our technology investments and despite the revenue decline from the pandemic. I'm proud of our team for this cost discipline in a difficult economic environment.

Fourth quarter capital spending was $394 million, and that included $29 million of capital to support the [integration] of ADS and about $30 million of capital that we intentionally pulled forward given the strong recovery in our operations during the third and fourth quarters. 2020 capital spending was $1.632 billion. Our team showed tremendous discipline throughout 2020 as we focused on reducing capital spending in a targeted manner given the volume declines from the pandemic.

Waste Management generated free cash flow of $2.656 billion in 2020. Given the significant impact of the ADS transaction on this result, let me provide detail on some of the moving pieces. After-tax proceeds from the divestitures of ADS and Waste Management businesses to GFL were $691 million. These proceeds were partially offset by after-tax transaction and advisory costs to support the acquisition of $117 million. Normalizing for these 2 items, 2020 free cash flow was $2.082 billion. This result demonstrates the resilient nature of our business and the strength of capital discipline as we nearly achieved our original 2020 free cash flow guidance of $2.15 billion despite the impact of COVID-19.

Given the strong result, at the end of 2020, we were positioned to forgo relief provided by the CARES Act, and we elected to pay approximately $120 million of payroll taxes that we had planned to defer. As we repay that amount in 2021 and 2022, as anticipated, 2020 free cash flow, excluding the ADS impact I mentioned, would have been about $2.2 billion for the year, which is better than we expected at the end of the third quarter.

In the fourth quarter, we used our free cash flow to pay $231 million in dividend. For the full year, we returned $1.33 billion to shareholders, comprised of $927 million in dividends and $402 million in share repurchases. In November, we issued $2.5 billion of senior notes at an extremely attractive pretax weighted average cost of less than 1.5%. This allowed us to repay short-term borrowings used to fund the ADS acquisition at close. 2021 cash interest savings are expected to be more than $90 million.

Fourth quarter total debt-to-EBITDA of 3.19x and forecasted leverage ratios are both well within the financial covenants of our revolving credit facilities. We are committed to returning to our long-term targeted range of 2.5 to 3x total debt-to-EBITDA during 2021. Our balance sheet and liquidity remain strong, and we are well positioned to continue our practices of sound investment and strong shareholder returns.

Moving to our 2021 outlook. As John mentioned, we anticipate 10.75% to 11.25% revenue growth in the year ahead with solid organic growth in the collection and disposal business of between 4% and 4.5%. This underpins our 2021 operating EBITDA guidance of $4.75 million and $4.9 million. We expect this strong earnings growth to drive free cash flow of between $2.25 billion and $2.35 billion.

Capital expenditures are expected to be between $1.78 billion and $1.88 billion in 2021. Excluding about $90 million of capital planned to support the ADS integration, this expectation is in line with our long-term capital spend as a percentage of revenue target of 9.5% to 10.5% even while we step up our investments in CSD.

As Jim mentioned, we also see potential incremental investment opportunities in our recycling and renewable energy businesses, both of which aid in our sustainability efforts and generate strong returns. As we've now seen improved returns in our state-of-the-art MRFs, we are taking plans to deploy the latest technology and additional MRFs in our network and moving those forward. We're also planning to invest in more renewable energy plants at our landfills. This investment extends our ability to close the loop between our renewable energy plant and our CNG fleet and does so with very strong economic returns for the company.

We remain committed to a capital allocation plan that maximizes long-term value and total shareholder returns. As announced in December, we are pleased to be increasing our planned quarterly dividend for the 18th consecutive year. We expect our dividend payments to be about $975 million in 2021. Given our focus on the ADS integration, we expect tuck-in acquisitions to be on the lower end of our typical range of $100 million to $200 million. With more than $1 billion remaining from our free cash flow guidance, we plan to allocate that to a combination of debt repayment, share repurchases and the high-return, sustainability-focused, capital investment opportunities I described earlier.

In closing, I want to thank the Waste Management team for their dedication and adaptability to overcome the unique challenges of 2020. We are stronger than we were a year ago, and we're looking forward to a better 2021.

With that, Lara, let's open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question will come from the line of Hamzah Mazari from Jefferies.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

My first question is just on the volume side. What are you guys seeing on commercial service increases today, how that's trending? And then in the 4% to 4.5% organic growth, do you -- are you baking in any vaccine impact on volume? And how should we think about that?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. Hamzah, first, as far as service increases go, we looked at the fourth quarter as being really good news because it's the first quarter in a while that we've seen net service increases. We were negative, of course, in Q2 and negative in Q3. And so we turned positive in Q4, and that's very good news as it relates to -- particularly as it relates to small business.

And then as we think about volume overall, I think what we -- most macroeconomists are saying that the economy recovers as the vaccine rolls out. And so volume is the one that is hardest for us to predict. Normally, it's fairly predictable for us, but it's hardest to predict this go-round because we don't know how quickly the vaccine rolls out. But we are starting to see some encouraging signs from states that we talked about previously that were lagging. States like Illinois, Michigan, Pennsylvania are starting to show some signs of recovery. There are some states like California, New York and then also provinces like, I would say, Ontario and Québec that are still way behind. But -- and then, of course, the states that have been -- that opened first, like Texas, like Arizona, Tennessee, Florida, those states have been doing actually reasonably well. So our expectation is that those states that are starting to reopen and even the states that haven't started will start to perk up here. And we think that we'll be back to some sense of normalcy on the volume front in the back half of 2021.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

Got it. That's very helpful. And just any comments or thoughts around the new EPA head? And any changes you see regulation-wise that could impact your business from sort of the Biden administration, whether it's PFAS around leachate, whether it's renewable tax credits increasing? Historically, I think you've been able to pass through environmental regulation costs as a fee. But just any thoughts around that? And is the increased investment in MRFs and landfill to gas, is that linked to what you see coming out of the EPA at all? Or you would have done this anyway?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

So I'll take the last one first. Not really related to what we're seeing coming out of the EPA. First of all, it's very early in this new administration. So those investments are really related to the fact that we believe from an ESG standpoint that they are the right thing to do, but we also believe that they provide great shareholder return. So -- and we've -- this is not something that came to us in the last 3 months. I mean we've been investing in these renewable plants on a -- and doing it diligently over the last probably 4 -- 3 to 4 years. And then, of course, the recycling business is also related. But we do think that there is a nice uptrend starting, and it will continue. And we believe that it's not your normal ebb and flow in terms of commodity prices. It's why I said in my script I think we're disproportionately affected by this in a good way.

So your first question really relates to what our expectations are coming out of the new administration. And in an odd sort of way, Hamzah, we feel like more, I guess, greater regulation is actually a good thing for us because we hold ourselves to a higher standard than the baseline regulations. Whether it's from EPA or whether it's from state DEPs, we hold ourselves to a higher standard. And so therefore, greater regulation actually ends up being a differentiator for us. And while we don't know exactly what will come out of EPA in the form of regulation around things like PFAS or coal combustion residuals, things like that, we do look at this as being an opportunity. So we're not displeased with what the future holds for us from that standpoint.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

Got it. Just a clarification question, I'll turn it over. Are you guys guiding EPS? Or is that sort of not part of guidance anymore? I'm just curious if there's a change in guidance or maybe we missed it.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

We didn't guide EPS, and I don't think we did last year either, Devina.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

No. And the real thing there, Hamzah, that we're focused on is purchase price allocation impacts to depreciation are difficult to predict. And while we have a really strong view of the purchase price allocation with our 12/31 close, that's something that can get adjusted throughout the next several months. And so the depreciation impacts are something that we'll get better clarity on over the course of the year. But that's one of the things that created noise in EPS and one of the reasons we elected not to guide on that front.

Operator

Your next question will come from the line of Kyle White from Deutsche Bank.

Kyle White - *Deutsche Bank AG, Research Division - Research Associate*

I wanted to talk about ADS and just kind of see how the integration is going. Anything in particular, better or worse, than you expected about the assets now that you own them?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Kyle, no, I think I would tell you 90-plus days in, I think we're right on track. I think there's been no real surprises. The things that we've encountered have all been things, frankly, that we've contemplated. We did have the benefit of a longer time frame getting ready for it. But I would tell you that I think we're exactly where we should be, in fact, probably a little bit ahead. As you heard in my script, the one area that will take total Q2 to get going in terms of synergies is on the routing side, and that has as much to do with data and system migration as it is anything else. And in addition, there's some technology improvements that we're making right now in the ADS fleet to be able to take advantage of all the processes that we have in place to drive efficiency. But I would tell you, I'm very, very pleased with where we're at so far.

Kyle White - *Deutsche Bank AG, Research Division - Research Associate*

Got it. And I know it's still ongoing in a very sporadic situation, but do you have a sense of the impact that this extreme weather is causing to your volumes or maybe increased cost of the business?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I would tell you, certainly, in the Houston area right now, it's been a rough couple of days, and this is not nearly a part of the country that deals with this kind of stuff very well as evidenced by what's happening here. But I think outside of Houston, we don't have a real feel for what is going to -- how significant it's going to be going forward outside of really Texas.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I wish I had a sense, Kyle, of what -- of the damage to my house because I have a little bit of damage at the house, so.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

It'd be great to know when power and water are coming back.

Operator

Your next question will come from the line of Tyler Brown from Raymond James.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Devina, so thank you for all the guidance. It's very helpful. So as I look at the guidance and I think on my math, you're looking for something like 10 to 20 basis points of margin expansion in '21, if my math is right. My feeling is there's quite a bit moving around in there. Can you just talk about the puts and takes on margins from a year-over-year basis, maybe thinking about core expansion, maybe how much recycling is going to help and then maybe how dilutive M&A might be?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Certainly. So -- and you are absolutely right, there are puts and takes, but we still see good strong margin expansion on that path toward 30% that I know that we consistently talk about. The organic revenue and EBITDA growth of our core solid waste business, we see improving 30 to 50 basis points in the year ahead. That is going to be partially offset by some known cost headwinds and then also a very intentional increased technology spend level. The increase in technology spending specifically has about a 30-basis-point impact on the margin measure and about a $50 million impact on EBITDA dollars.

In terms of the other puts and takes, I would say recycling from a margin perspective isn't actually one of the things that's contributing to the margin either expansion or detraction. And that's because for us, we have the recycling brokerage business, which tends to offset the margin expansion that we see in the traditional MRF business. So as we see the operations improve on the MRF side, we tend to see a little bit of dilution from growth in our brokerage business, which is a very good return on invested capital business for us, it dilutes margin.

On the renewable energy side, there will be some margin expansion, and that was strong in the fourth quarter and something that we are basically including in our 2021 guidance based on how we finished the fourth quarter of 2020. So potentially some upside there if we see RINs prices continue to escalate from where we ended the fourth quarter.

And then with regard to the ADS acquisition, I want to pause on that one for a moment. Fourth quarter EBITDA margin was 18.5% for the ADS business. That's below their run rate of 24.5% on a WM measurement basis. As a reminder, ADS's EBITDA margin included some adjustments for both share-based compensation and accretion that Waste Management doesn't take in its own EBITDA measure. So on an apples-to-apples basis, ADS's margin was 24.5%. And we have strong confidence that we'll get them up to about 28% in 2021 and then continue the march to WM levels from that point on.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Okay. Extremely helpful. Real quickly as well from a modeling perspective, so I think you mentioned you paid the $120 million in CARES back. I'm just unclear, is that just the half that was due for '21? Or does that repay the burden for both '21 and '22?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

That repays the burden for 2021 and 2022. So the entire $120 million that we had been deferring over the second and third quarters was repaid in Q4.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Okay. Awesome. And then, John, I know we've talked about resi margins quite a bit in the past. In 2020, did resi margins improve as you refocused there? It sounds like they did. And then secondly, how long do you think it takes to get that business back to either, call it, a more historical margin level or maybe a level that you would be more happy with?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Well, what I would tell you is how in my prepared remarks we talked about $40 million of benefit being generated in that line of business in 2020. I would tell you, we still obviously have work to do in 2021. I don't -- we're not going to get there in 2021. And frankly, some of the other hills we're having to climb around COVID and the weights, hopefully, that's going to moderate in the back half of the year as things -- as Jim mentioned, if vaccines get out there and things start to moderate to whatever -- to normal. In the back half of the year, we're also going to have a better view of what the residential weights are going to look like long term. What I would tell you is not lost in that mix is the fact that our price and yield in residential continues to be strong despite what's going on with CPI, and we've talked about that for the last handful of years.

And the other part that's part of that equation is while we talk about the recycling business improving a big piece of, the recycling business affects residential. So when you look at those margin improvements, we're overcoming some of those other headwinds that weren't there when we started this initiative, so to speak.

Operator

Your next question will come from the line of Kevin Chiang from CIBC.

Kevin Chiang - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

Maybe just turning to one of your prepared comments around, I guess, you're seeing an acceleration in some of the technology initiatives you had. I think you called it a triple-digit rate increase in your online sales channel, for example. If I recall, at your Investor Day, you kind of laid out a bunch of technology initiatives. And I think in aggregate, that was going to generate $150 million of savings or kind of earnings opportunities. Just as you stick here today through the pandemic, do you see the ability to achieve that coming sooner? Is the upside potential potentially bigger, just given maybe the change in some of your customers' behavior through the pandemic?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. So to answer that question, at least it's hard to say whether it is a bigger opportunity for us. But because we've chosen to accelerate it, then you would expect that the impact would happen sooner for us. And we're touching really -- I mean, this is a huge transformation for us. I mean we are literally digitalizing the entire relationship from the very front end, which is where we set a customer up all the way through the routing and dispatch and then collection functions and all the way through billing and the back end of the process. So it's a massive effort for us, but it don't like it was the right thing to do to accelerate it.

And so when we talked about that on an Investor Day, I would tell you that that's -- that it would makes sense that by accelerating the spend, we would also accelerate the benefit. I don't know whether the benefit is necessarily bigger because some of that is dependent on how much differentiation we create. And that is maybe less dependent on us and more dependent on whether competitors choose to do the same thing. But we do believe that having an end-to-end customer experience that's digitalized is something that's almost becoming just the ante to get into the game anymore. It seems as if every company that did well in Q2 when this thing hits where digitalized in some way, shape or form. And so we felt like this was absolutely the right thing to do for our customers. And we do believe that it gives us an opportunity to grab a bigger slice of the overall pie, particularly with those away from competitors that don't choose to make those investments. We know that some competitors already are making those investments or will be. But that piece is maybe a little harder to quantify.

Kevin Chiang - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

That's helpful. And maybe just turning to your long-term debt or your leverage ratio, you're looking to get that back to 2.5 to 3x. But I guess, if you take a look back, I mean, a lot of your comments around the resilience of the business, the -- you outperformed the kind of expectations as you go through a challenging year. Just wondering how you think about your capital structure and if there's an argument that maybe 2.5 to 3x might be suboptimal for a company given the resiliency you have in your underlying earnings stream. Just like how do you think about that in the context of what you've gone through in 2020?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

I think it's a great question, and there's no doubt that producing the free cash flow and EBITDA that Waste Management did in 2020 in the face of a global pandemic is a strong affirmation of the strength and resiliency of this business. And so arguably, it certainly could position Waste Management to consider a higher leverage ratio than we had historically. That being said, our focus on that long-term range of 2.5 to 3x is both considering through-cycle financial position that we look to achieve and also establishing financial flexibility for strategic opportunities. And so we want to be sure that we aren't just positioned to weather a storm, so to speak, but that we're also positioned to be opportunistic to grow the business over the long term. And that's why we think that 2.5 to 3x is the right level for strategic value for value creation for shareholders.

Operator

Your next question will come from the line of Jeff Goldstein from Morgan Stanley.

Jeffrey Daniel Goldstein - *Morgan Stanley, Research Division - Research Associate*

In your prepared remarks, you mentioned commercial yards and industrial hauls declined 5% to 6%, but overtime declined between 15% and 18%. I was just curious, what are you doing to drive that delta? And how we should think about the sustainability of that delta in the future?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Well, I think, Jeff, in terms of sustainability, when you really look at where we bottomed out in Q2 and then you look at Q3 and Q4, while the volume declines have essentially been cut by more than half, we've still been able to keep a proportionate amount of overtime. And it's really just us being really focused on making sure as volumes fluctuate, we optimize each day and each week when it comes to the people and the assets. The operating team is doing a really good job of holding on to that as we bottomed out. And then as we've come back, we've just been able to maintain that same level of discipline about making sure that we're maximizing each day and each week on an asset basis.

Jeffrey Daniel Goldstein - *Morgan Stanley, Research Division - Research Associate*

Okay. Got it. And then thinking to the 2021 core price growth guidance of 4%, can you parse out your expectations across commercial, resi, industrial and landfill? Will the price increases being relative lockstep? Or are there some areas you expect to see more strength relative to others?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Well, I think if you look at the trend -- we didn't break it out by line of business. But I think overall, if you look at the trend from, again, where we bottomed out to where we finished the year, the second half of the year, Q3 trends into Q4, I think you follow those forward proportionately with each of the lines of business. So one area Jim commented on in his script was really around post-collection pricing, both at the landfill and transfer station. We've talked about that quarter-in and quarter-out. We continued even through the pandemic to show strength and resiliency in those 2 buckets. And I commented on residential, and that has been, even pre-pandemic, a real focal area for us. And while it did moderate a bit in the bottom of the pandemic, we've shown progress out of that. So I think we feel comfortable with at least that 4% going into 2021.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Jeff, the one thing that has been the most challenging for us has been that commercial line of business because it's so impacted by small businesses. And it's also impacted by hospitality. It's impacted by schools, in addition to small businesses. It's why we like the industry, honestly. As you think about an investment thesis, it's why we like -- we're more of a reopen play, this industry is, than we might have been in the past. Because we haven't gone through something like this where everything is shut down and, in many cases, are still shut down. So whether it's WM or whether it's any other waste provider, this is a -- this industry is a reopen play, and that shows up on the pricing line as well as the volume line.

We have some of the price that might be perceived as being somewhat soft in the commercial line of business, is really because it's volume-related price. I mean it doesn't feel morally right to use our fee-based approach, which is a new approach for us, but it's -- and it's a sophisticated approach. But you can't go and hit small businesses that are sitting across the street from Wrigley Field and who are typically customers that have a burging business during the baseball season, and now they have nothing because there's no fans. You can't hit those customers with fees or with price increases. And they understand that, and we understand that. They also understand that when their business reopens, that we will increase prices as we normally do, normal course of business.

So there are some volume-related price increases that we simply haven't taken, and that specifically impacts that commercial line of business. Other lines, as John talked about that are doing quite well are landfill and transfer. Residential, obviously, has gotten a lot of focus. So we feel very good about pricing. And there's been absolutely no loss of discipline. That's hard-coded here. It's just that there's -- that we're waiting for some of this volume to return before we feel like it's the proper time to really reapply.

Operator

Your next question will come from the line of Jeff Silber from BMO Capital Markets.

Jeffrey Marc Silber - *BMO Capital Markets Equity Research - MD & Senior Equity Analyst*

In prior quarters, you had given us some color on your commercial and industrial clients in terms of service status, what percentage of those customers have come back, what percentage are not coming back. I'm just wondering if we can get an update and what you think we should expect for the rest of the year.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Yes. Jeff, we said we were probably in the high 60s, approaching 70% the last time we chat. And I would still tell you we're hovering a little bit better than that, right in the 70% range. And as Jim mentioned, the real gap there is just around those businesses have to return. It's really hospitality, the reference to Wrigley Field, travel, lodging, those kind of things. So I think the good news is that if you look at how well the business performed even without a lot of those small businesses being back online, we feel very confident. As those businesses come back, we'll emerge from this even stronger. I would tell you, we're -- when you look at our margin performance relative to that as well, I think that's also a testament to how well we performed. And as Jim said -- to Jim's comment, this is a reopening story, I think, for the industry and specifically for us. We feel very confident about how the business performs as things start to reopen really in the back half of the year.

Jeffrey Marc Silber - *BMO Capital Markets Equity Research - MD & Senior Equity Analyst*

All right. That's great to hear. My follow-up question. You talked earlier about some of the potential regulatory issues from the Biden administration. I want to focus on something a little bit different. There's a proposed federal minimum wage at $15 an hour. I realize you can probably pay more than that. But when we've seen minimum wage increases in some of your territories, some of the states, some of the cities, has that put upward pressure on wages for you? And if so, are you able to pass that through to your customers?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. I think it's a great question, and it's one that we've been evaluating. I think the most important element of this for us is that we've been a competitive wage payer as a company for many years. And so while a minimum wage could certainly effectively raise the tide with regard to where wages are, we see that as something that wouldn't disproportionately impact our business and instead is something that we are ahead of in many respects because of where our wages have been historically. It's certainly something that we see the ability to consider if we see that raising -- that rising tide impacts our cost structure, it's something that we would respond to on the price side of the business.

Operator

Your next question will come from the line of Noah Kaye from Oppenheimer.

Noah Duke Kaye - *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Jim, I just want to pick up on what you were saying previously around some of the pricing considerations related to volume coming back. And it's really about sort of how pricing and yield cadence might trend over the course of the year. One might think that just because first half of 2020 yield comps are a little bit easier relative to the second half and you have the CPI headwind in the back half of the year that you would see better pricing in the front half and ease off in the back half. But it sounds from your comments like there may be just more open-market pricing power you envision later in the year, and so perhaps pricing will be more ratable. Is that a fair way to think about it? Or can you steer me properly?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes, I think that's a fair way to think about it. I mean we have different approaches to different lines of business. So landfill and transfer, honestly, had not gotten the focus that commercial has gotten until probably 2 years ago. So we've been very focused on landfill and transfer pricing. And so similarly, we've been very focused recently on residential. And John has talked about that probably for the last 4 quarters.

I think commercial is, as I said, it's -- we've really established a more sophisticated-based approach to commercial pricing, but we do have a significant percentage of those commercial customers that are small businesses. And one that we didn't mention necessarily this morning, but it is schools. I mean schools are, I think, make up 12% of our commercial business. And in some states -- and I hate to even think about this, but in some states, schools haven't returned. So -- and that's grade schools, that's high schools and that's universities. That's a big part of our commercial business. It's a part of our industrial business as well. But when it's 12% of your commercial business, it makes a difference. And you're simply not able to price increase customers who either haven't returned or have returned sparingly. So we think schools are a huge focus at the state level and the federal level and that they -- so the kids need to get back into school, and so I think you'll see the schools reopen fully as we get through the vaccine, and we see that at the back half of the year.

Noah Duke Kaye - *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Yes. And I want to talk -- that really sets up a more medium-term to longer-term question around the cycle here. I mean one would look at the typical indicators, very robust housing starts activity, God-willing, a full year of reopening in 2022. And then it certainly looks like CPI is going to be higher for '21 versus '20. Does it seem right to you that we may have some acceleration of growth in 2022? And how are you aligning the business for that, if so?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes, that sure seems like a logical conclusion to me. I mean it feels like this economy is ready to really take off like a space shuttle. And so we're seeing some indications of that. Probably, our C&D line of business from a volume perspective is the best indicator. That had been down, way down in Q2, I mean, double digits down. And for the fourth quarter, our C&D volume in Orlando was up 5.5%. So that's starting to tell me -- and that's probably one of the best leading indicators that we have in terms of volume, that tells me that things are -- or the pump is primed, and it's ready to go.

Operator

Your next question will come from the line of David Manthey from Baird.

David John Manthey - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Was hoping you could update us on the current levels and your year-end 2021 targets for the percentage of municipal contracts that are linked to a more representative water, sewer, trash CPI index as well as fee-for-service recycling contracts.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

So what we've traditionally said is about 40% of our revenue is somehow indexed. I think the better metric to look at is really what we've done on core price and yield within residential over really the last 6 or 7 quarters. I'm looking at Devina to make sure. We've shown progress in each and every quarter, including 3 to 4 and throughout 2020, and we expect that absolutely to continue in 2021.

We -- I did mention in my prepared remarks that we did shed a little bit of business here in 2020. But as I've mentioned in a number of these calls, if it doesn't meet our margin and return criteria, we're comfortable doing that. It's not our intent, but we're going to make sure that we deploy our capital to where we get the -- get reasonable returns and margins.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I'm not sure, John, of what percentage -- we can get to the percentage for water, sewer, trash. Suffice to say, it has gone up. In fact, we've seen -- I've seen a couple of contracts come across my desk where we are -- where we won the bid, and we've increased them off of some of these indices that really weren't representative of our cost structure to water, sewer, trash. But I don't know, John, the exact percentage. We can get you that percentage for you.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Yes. And we'll circle back with that number.

David John Manthey - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. And then as you work to get the highest cost mile off the road, for modeling purposes, is it more relevant to compare overtime trends in 2021 with maybe 2019? And if so, what would -- is like a 5%, more or less, kind of decrease something that would be reasonable just given the wild swings we saw in overtime in 2020?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I don't know if I'd go back to 2019. What I would look at is where we bottomed out in Q2 and what our overtime percentages we're going into that and how we've come out of it. To me, that's really been the barometer as this volume declines have really come back more than half in commercial and industrial. As for obvious reasons, residential is a little different. But we've been able to outpace the volume increases, if you will, from an overtime perspective for us to be down mid-teens and overtime with still 5%, 6%, 7% volume declines is pretty impressive. So I don't know about 2019. David, I think the better barometer for us is how we've done in 2020 and how we progressed from the peak of volume decline to where we are now. And I think, as I mentioned, that's what gives us confidence going into 2021 and then add in the benefit of us getting into the integration of the ADS customers after we migrate the data here in Q2. All those things, I think, add up to a really positive outlook for us on the OpEx side.

Operator

Your next question will come from the line of Sean Eastman from KeyBanc Capital.

Sean D. Eastman - *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

I just wanted to dig in on the kind of the free cash flow bridge from 2020 to 2021. I mean, again, quite a few moving parts. It seems like we should be building off of a $2.2 billion number in 2020 in essence. But Devina, maybe if you could just kind of give us a simple kind of rundown of that bridge and those moving parts from a free cash flow perspective, that would be great.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. So the $2.2 billion that you remark on is a good place for us to start. I think when we think about EBITDA growth always being the biggest contributor there, certainly, have strong outlook for EBITDA in the year ahead with a 10% to 13.5% increase on a year-over-year basis. In addition to that, we expect the about $90 million benefit from lower cash interest that I mentioned. Cash taxes will increase with those 2 items going in the opposite direction, and we estimate that to be about $125 million to $150 million. There will be a benefit from the fact that the company paid the transaction cost that is in your $2.2 billion base. So I want to be sure to point that out because the ADS transaction costs are something that we adjusted for and coming to that $2.2 billion. We will have a slight increase in the money spent on the enterprise resource planning that we've discussed. We expect that to go up $15 million on a year-over-year basis.

So all in all, that's what gets you to your cash from operations increase in the ballpark of $500 million to $600 million. We've got a capital expenditure increase of around $150 million to $250 million. And then proceeds from divestitures, we're not forecasting anything significant there, have given our traditional range of $50 million to $100 million.

Sean D. Eastman - *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

Okay. Super helpful. And next one for me is just on RNG. It sounds like this is going to be a growing piece of the business. And it'd be helpful maybe just to get some context for how significant of an earnings driver you foresee this being in maybe 5 to 10 years. And maybe as of today, is there a rough idea on what the sensitivity in EBITDA is to RIN prices today?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. Probably all 3 of us could take a shot at this one. I'll go first, and then I'll just pick up the pieces after I pull this up. But I think -- look, I think it depends a little bit on -- to your first question, it depends on how we choose to grow this business. I mean you could make a case that you grow this business outside of our own balance sheet. And so we are -- we have not gone down that path, but if you wanted to really kind of blow out this business in a good way and take advantage of what we think is going to be a long-term trend for RINs pricing, you could do that, or we can grow it within our own business, within our own balance sheet. And so we haven't made a decision there. Obviously, to date, everything has been grown out of our own capital expenditures. So -- and anything that we're contemplating probably at least for the first half of '21 would -- and maybe for the entire year would be grown through capital expenditures, as Devina mentioned in her prepared remarks.

But we do think that this is a -- as I said, there's a long-term uptrend here for commodities. And so that's why I believe it benefits us disproportionately regardless of where you look in our earnings stream, whether you look at renewable energy with $2.50 RIN pricing or whether you look at our recycling business where we're the biggest recycler out there. We feel like this is a more of a 3- to 5-year trend. There's a number of reasons for why we see that. I mean here's -- commodities obviously have been a pretty heavy ebb, if you will. And so -- but if we look just at our own business, we see that there is increased demand for cardboard, for example, that's driven by what we've discovered in the pandemic that everybody is taking delivery of Amazon boxes at their houses.

So we feel like all of these businesses that have commodity price exposure looks to -- they look to have a fairly long uptrend coming. And that's why we are excited about the prospects of whether it's our recycling business or our renewable energy business. And that renewable energy business, by the way, is made possible by the fact that we have 60% to 70% of our fleet is natural gas. And that also is something that can't be matched in the industry percentage-wise. I hope that helps answer some of that. John?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

The only thing I would add there with the new administration, I think 2 things that the new administration will deal with is the RVO, which is a renewable volume obligation, and a small refinery exemption which are 2 buckets that have really driven RIN pricing in the past, right, because there's been a lack of clarity on that. And I think if they stabilize both of those, we're going to see some more stability in RIN pricing, whether it stays at $2.50 or whatever. But I think we'll see more stability, and I think that's going to help inform us where we deploy our own capital.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

And EBITDA for the renewable energy business was up about $50 million in 2020. What's important to note is that, that wasn't all price-related. Some of that was our intentional investment, as Jim mentioned, that we've been making over the last 3 to 4 years. So there was volume and price acceleration in 2020 that provided about $50 million of EBITDA growth. And we see about a $10 million to $15 million improvement in 2021 based on where RINs prices were at the end of 2020.

Operator

Your next question will come from the line of Michael Hoffman from Stifel.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

I want to just touch on the service interval trend assumption in your model. What I think I heard correctly is you did -- you had a favorable improvement in 4Q, but you're not assuming it continues to improve favorably. It's stable, and therefore, that's upside if the housing cycle converts into new business formations.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

The way that I would look at that, Michael, is our volume guide at the macro level for 2021 is about 1.5% volume growth. Clearly, a lot of that is built into the second quarter, just coming off of the very low base of Q2. We do see some upside in the back half of the year. From a service interval perspective, I wouldn't say that we took that volume guidance to the different parts of -- different lines of business specifically, such that I can bifurcate what of that is commercial or industrial. But what we looked at based on how our cost structure responded in 2020, we think that the contribution margin of that volume is around 45% in the year ahead.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Michael, to one of the earlier questions about, does the economy feel like there's a lot of momentum behind it that's ready to really take off? Once we get past this, I think the answer is yes. We just -- because we don't have a ton of control over that. That's the one that we don't have really much control over, which is volume because of this -- when the pandemic starts to -- the effects that start to lessen. So if your question is about is there conservatism in this volume forecast of 1.5%? I would tell you that the answer is probably more likely yes than no, but it's -- it is largely dependent on when this reopening comps. But as I said to the earlier question, I absolutely believe that that's a logical conclusion that this economy will be ready to take off once we get past it.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Right. And yes, that's where I was getting to is, the history is household formation drives new business formation. We're at $1.5 million and change start, $300,000 more than it's been for 5 years. At some point here, the empty storefront gets backfilled.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

That's right.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

You needed a dry cleaner. You need another drugstore or what have you. And that's a box, and that's service interval growth. That was the way to think about it.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. That's right, Michael.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Just to be clear, cadence-wise, based on how you ended the year, here, it looks like you could actually be flat. It's just barely negative on volume in 1Q and then have a nice pop and then settle into a lower-but-sustained trend in the second half. Am I thinking about the cadence correctly there?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Michael, I certainly can do the math and get there. I think we saw lull in late November and December. But the good news, as I mentioned earlier, is that through the first 6-or-so weeks, been encouraged by what we've seen on the volume front. Now 6 weeks does not make a trend. But to your question and relative to Q1, we feel pretty optimistic through the first 6 weeks anyway, in terms of volume.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. And Devina, if I could try a different tack on a waterfall on 2 things, the EBITDA and the free cash. In the year at 4, 3, I'm rounding, you guided to 4 8. It looks like Advanced would be about 2 60 incremental. And you get recycling, John mentioned 45. You mentioned 10 to 15 in RINs. That leaves me like 190 coming from solid waste. Have I thought about that sort of the pieces in the right zone there correctly on the EBITDA to go from 4 3 to 4 8?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

So we have expectations for the ADS business a little north of what you just projected. We have the $50 million increase in technology that I mentioned earlier that is not part of your bridge. And then we have the known cost headwinds that I mentioned. So you can think of those being specifically related to health and welfare costs, risk management costs and incentive compensation. Those are about $100 million in the aggregate. So those are the pieces of the bridge in addition to what you outlined.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. And then I'm just trying to piece together the question that was asked earlier about the free cash flow one. So it seems like you'd started at $2.082 billion because you paid the CARES Act back. So it's -- that's gone. And you're going to 2 3. That's $220 million roughly year-over-year net. But the absolute is actually closer to $300 million because you've got about $100-and-some million of cash tax and the like ERP. So I'm really -- I'm looking at a sort of a gross $300 million improvement and then offset by some cash tax issues and ERP. Like is that -- did I get -- did I pull those pieces together about right?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. Yes, you did.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. So last one, and I know you and I do this all the time, you wants to find your baseline free cash is $2 billion. And I just want to ask is, am I looking through the lens correctly on what I think your own self-help opportunities are that ADS brings in $150 million to $200 million. Eventually, working capital has the potential for $150 million to $200 million. IT is another $75 million. So there's a $375 million to $475 million baseline upside. I get it might take a couple of years to get all of that before I even introduced 5% to 6% annual recurring growth in the cash. Am I thinking through this correctly? And if I am, all of that self-help, I don't need anything to happen in the macro. That's something you can do.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. The only thing -- so I agree with you 100% that working capital and ADS free cash flow, flow directly to free cash flow. The technology additions that we've mentioned, you would have the tax effect. That's the only other item that I would clarify on what you just did. But otherwise, I think we're in the same place.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

And then I'm not sure, Michael, how much of kind of -- I mean, your very first question is factored into your math there, which is an economy that grows at a faster pace than the normal economy because of this reemergence. I don't know how much of that's in there, but we do believe that's real. We just haven't put it into 2021 yet.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Yes. Well, that, to me, just takes your baseline growth rate of -- if it's 5 6, it turns into a 6 to 8. That's what I think.

And lastly, would you talk to us about how inflation influences your business model? I think it's a positive. I'm in the camp that you love inflation, and that just helps pricing leverage. But can you talk about that?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I guess it's -- I'm not sure I would say I love inflation. But yes, I get your point. I mean we are good at passing it through, through our pricing mechanisms. And so while we -- and look, maybe the best example of that has been landfills where we've seen inflation on the cost side of our landfills for probably 2 years. And as a result, we've started to get quite a bit better on pricing at the landfill and at the transfer station. So we do expect that inflation has been extraordinarily low for quite a long time. I don't know that, that lasts for a lifetime. So I think we will see inflation tick back up, certainly on the commodity side. And -- but we will do a good job of making sure that gets passed through and then add some margin to it through pricing programs.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

And the thing I'd add to that is there's leverage on that as we see better execution with technology to optimize the back-office processes we've talked about as John and team drive the organization to be more efficient on the road every day. So we've seen tremendous operating and SG&A leverage that helps us to combat inflation. And so those things give us leverage in an inflationary environment as well.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Right. That offsets your internal cost inflation and then the incremental leverage on inflation to your price spread just drives incremental margin expansion and free cash flow growth.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Absolutely.

Operator

Your next question will come from the line of Michael Feniger from Bank of America.

Michael J. Feniger - *BofA Securities, Research Division - VP*

Jim, just following up on Hamzah's question around the new EPA and the PFAS question. There's obviously a lot of headlines around super fund sites and designation of the chemical and liabilities and lawsuits. Is there any direction or regulation you're specifically looking for or that we should keep an eye out for that would sway things a certain way? Or is it just kind of status quo in terms of your investments there and what you guys have been doing for the last few years?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. Michael, I think it's probably -- it's still a little bit early in that game. There's a lot of discussion around PFAS, but -- so I'm not sure that -- it's not that we don't have a strategy from a lobbying standpoint. We do have a team in D.C. that is looking at this closely. But I guess, the main thing I would say about PFAS is that while some people are looking at it as a cost, we're looking at it as an opportunity for us. I think it goes back to, I think, to the original premise of your question, which is if something changes environmentally through EPA as a result of the new administration and part of it might be PFAS, how does that affect us? And we think it actually has potentially a positive impact, and that's why we're looking at it as an opportunity as opposed to just a cost.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

And Jim, the one example I gave is if you think about contaminated soil. That's a place where this PFAS resides regularly. And we look at our landfills as being a perfect solution for that with the right technology on the back end.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Absolutely right.

Michael J. Feniger - *BofA Securities, Research Division - VP*

That was really helpful. That's good color. And Jim, just lastly, just I love to get your big-picture view on M&A. I mean the ADS integration is underway. The approval process was certainly longer than anyone expected. Some of your peers are expecting another sizable year of outsized tuck-ins. Just with so much consolidation underway right now, I'm just wondering if long-term M&A at Waste Management shifts. Are we shifting to find new markets for you guys to grow into outside of traditional waste with what's kind of played out in the last few years?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I guess that's possible. I mean, I guess, what I can tell you with 100% certainty is we're not doing any more big solid waste acquisitions because I -- part of the reason that this took as long as it did was COVID-related. Part of it was just the complexity of it. I mean it was a complex transaction in a space where both companies played a major role. We're #1 in the space and ADS was #4. So there was a lot of complexity. There was a lot of work to be done with DOJ. And so I really don't expect that at least WM would do another large solid waste acquisition in North America. We'll do tuck-ins. And to Devina's point, about $100 million is where we think we'll come in this year. So I think we can continue to do tuck-ins.

And then as far as our strategy for M&A going out, I think what we've all chosen to do is just really focus right now on the integration of ADS. And once we feel comfortable that that's been well integrated, then start to think about what acquisitions look like in the years beyond 2021, 2022.

Operator

Your next question will come from the line of Stephanie Yee from JPMorgan.

Stephanie L. Yee - *JPMorgan Chase & Co, Research Division - Analyst*

I just wanted to ask a question about kind of your longer- or medium-term growth algorithm. So I think at your Investor Day, you had laid out that average yield could be about 2% volume growth being about 2%, and that drives 5-some percent of EBITDA growth. I was wondering if maybe ADS or COVID has changed that algorithm or if it's too early to tell at this point.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. I would tell you it's too early for us to tell at this point. The one thing that we did and we've mentioned from the time that we laid everything out at Investor Day was accelerate some of the technology spend. And that acceleration of technology spend is one of the things that has kind of put a little bit of downside pressure on the growth rate in EBITDA that we had talked about, but we expect that to provide an acceleration of the returns coming as soon as 2022.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I would only add, Devina, that when you think about when and how we bought ADS, they were very similar to us in terms of the volume declines. They were suffering through Q2 and Q3. So as Jim talked about, in the traditional business being a reopening story, we think there's obviously some leverage of ADS business now tucked in reopening and us getting the same lift out of that.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Good point.

Operator

Thank you. And presenters, I'm not seeing any further questions from the phone line at this time. You can go ahead and continue, please.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Okay. Thanks. And just to wrap up today, look, there have been so many challenges in this year that we've all faced, and that, of course, includes -- and thank you, by the way, for all of your comments about what's going on in Texas this week. I mean, honestly, for those of us here, it felt like Hurricane Harvey part 2 a little bit. A lot of damage to homes, including my own house, and a big, big percentage of the state without power, without water, et cetera. Not sure that it needed to be that way, honestly, but it was.

And so I guess, the positive coming out of it is that it tells me that the human spirit is alive and well. We -- and we at WM, or in our personal lives, we take care of each other during these difficult times. And so thank you to all of our 50,000 teammates that's -- for all you do each and every day. And thanks to all of you on the call for joining us this morning. We'll talk to you next quarter.

Operator

Thank you, sir. Thank you so much, presenters. And again, thank you, everyone, for participating. This concludes today's conference. You may now disconnect. Stay safe, and have a lovely day.
